

THE EVOLUTION OF POLICY IN
CONTEMPORARY ONTARIO

1

R
REFERENCE

THE ECONOMIC TRANSFORMATION OF ONTARIO: 1945-1973

BY D. R. RICHMOND



HC
117
.06
.0685
no. 1

PREPARED FOR THE
ARIO ECONOMIC COUNCIL

Ontario Ministry of Treasury,
Economics and Intergovernmental
Affairs Library

75/3134

NOV 7 1975

LIBRARY

Ontario Ministry of Treasury, Economics
and Intergovernmental Affairs Library,
POST BUILDING QUEEN'S PARK
TORONTO, ONTARIO, CANADA

THE EVOLUTION OF POLICY IN CONTEMPORARY ONTARIO

SERIES NUMBER: 1

THE ECONOMIC TRANSFORMATION OF ONTARIO

by

D. R. Richmond

Ontario Ministry of Treasury, Economics
and Intergovernmental Affairs Library
FROST BUILDING QUEEN'S PARK
TORONTO, ONTARIO, CANADA

This is one of several studies prepared for the Ontario Economic Council. Although these studies are published under the auspices of the Council, the views expressed are those of the authors themselves.

Ontario Economic Council
January 1974

THE EVOLUTION OF POLICY IN CONTEMPORARY ONTARIO

*Series issued by Ontario Economic Council
January 1974*

1. The Economic Transformation of Ontario: 1945-1973.
by D. R. Richmond.
 2. The Protection and Use of Natural Resources in Ontario.
by W. R. Smithies.
 3. The Service State Emerges in Ontario.
by Vernon Lang.
 4. The Role and Place of Ontario in the Canadian Confederation.
by Joe Martin.
 5. Ontario 1945-1973: The Municipal Dynamic.
by Lionel D. Feldman.
-

HC
117
060685
no. 1

THE ECONOMIC TRANSFORMATION OF ONTARIO

TABLE OF CONTENTS

I The Evolution of Economic Policy 1

 Economic Growth . . . Population Growth . . .
 Transformation of the Production Process . . . The
 Response of Government . . . Federal Economic
 Policies .

II Ontario Economic Policies 11

 The Aim was Expansion . . . The Drive for Indus-
 trial Expansion . . . New Relation with Government
 . . . Regional Industrialization . . . The Budget
 Becomes Instrument of Growth . . . Reform in
 Policy Making.

III Fiscal Policy 23

 Guardian of the Province’s Credit . . . The Aim was
 Debt Reduction . . . 1950-1957: Fiscal Policy on
 Capital Spending . . . The Search for Revenue: 1957-
 1962 . . . Another Revenue Source: Shared-Cost
 Programs . . . The Emergence of Fiscal Policy.

IV The Increase in Provincial Government
 Expenditures 37

 Table I Provincial Net General Expenditures . . .
 Table II Population and Net General Expenditure
 . . . Table III Personal Income and Net General
 Expenditure . . . Table IV Expenditure by
 Functional Classification.

V Problems and Implications 47

 Economic Policy Objectives . . . The Division of
 Responsibility . . . Coordinating Mechanism. . .
 Tax Sharing . . . The Limitation of Provincial
 Fiscal Policy . . . Overloading



Digitized by the Internet Archive
in 2018 with funding from
Ontario Ministry of Finance

<https://archive.org/details/economictransfor00rich>

The Evolution of Economic Policy

by D. R. Richmond*

The period since the end of World War II has been a time of immense changes in the economic and social life of Ontario. Three factors stand out: (1) The growth in the productive capacity and output of all sectors of the economy; (2) The increase in the population and in its mobility with a resultant concentration in urban centres; (3) The shift in employment from goods to service industries.

Each of these factors is interrelated and each has a profound qualitative impact. The change since 1945 is not simply a matter of numbers. The transformation of the economy goes far beyond increases in population and gross product. It reaches deep into basic values, lifestyles, social composition, and attitudes.

* D. R. RICHMOND, was born in Toronto, B.A. Queen's University and M.A. Carleton University. Has worked in Government since 1958 at all three levels including the Premier's Office at Queen's Park and the Privy Council Office in Ottawa. Prepared this report while serving as the Senior Economist of the Ontario Economic Council. Research assistant, Metropolitan Toronto, Chairman's Office.

Substantial research assistance in the preparation of this book was provided by G. P. Allsebrook, particularly in marshalling financial and economic data from successive Ontario budgets.

These qualitative changes have, along with the sheer growth of numbers, placed accelerating demands on government for more public services and involvement.

Economic Growth

Writing in 1959, Hugh Aitken noted that the three periods of rapid economic growth in Canada—the 1850's, 1900-1913, and 1939 to the present—were predominantly influenced by external pressures. Any objective review of the economic development of Canada and Ontario in the postwar period would bear out that observation. A combination of forces, many external to Canada and some internal, multiplied each other to trigger the longest sustained period of economic growth that this country has ever experienced.

Despite the recessions of 1954, 1957-58, 1960-61 and 1970-71, the overriding strength of the economy continually pushed up incomes and accommodated a rapidly growing labour force with a minimum of dislocation. This surge of economic growth was the cutting edge of a quiet and unrecognized social and political revolution, the dimensions of which are now only vaguely understood.

One crucial aspect of this revolution was the acceptance of the concept of rising expectations. A whole generation has been born and reached maturity experiencing nothing but affluence and rising incomes. If the depression generation looked for economic stability as the criterion of success for public policy, the generation coming of age in the postwar period expected a rising material standard of living.

Another aspect was the impact on government and on the role of government in an industrial society. The post-1945 period finally witnessed the demise of *laissez-faire*, the adoption of Keynesian policy, the introduction of economic, social and physical planning, and the steady expansion of government spending as a proportion of Gross National Expenditure.

A third, and dismaying factor, has been the persistent and sometimes rapid deterioration of the value of the dollar. There were three periods of excessive price rises—1947-51, 1956-58 and 1966-71.

The outstanding feature of the period, however, was the growth of employment and personal incomes and the resultant rise in material standards of living.

Population Growth

Paralleling the explosive growth in employment, output and incomes, and contributing to that growth, has been the expansion of Ontario's population. Three factors—rising birth rates, falling mortality rates and net immigration over emigration—all contributed to population growth until 1960. As a result Ontario's population was increasing at more than 2.8 per cent annually between 1945 and 1960. The decline of birth rates after 1960 and the fall-off in immigration near the end of the decade resulted in a slower rate of increase—2.1 per cent yearly in the Sixties. Nevertheless, the expansion of population in Ontario was larger than in Canada as a whole, and faster than in any other industrialized country in the world.

Immigration, accounting for almost one-third of the population increase, created unprecedented pressures on the capacity of the economy to supply the needed housing and related services. Canada and Ontario simply did not have the ability to provide the savings necessary to keep pace with all the demands for social capital, and at the same time finance the industrialization of the economy.

This problem was aggravated by the shift of population from rural Canada to the cities. Urbanization of the population, which was concentrating in metropolitan centres, accentuated the demand for housing, water and sewage works, roads, hospitals, schools and a full range of urban public services as well as large scale commercial and industrial investment.

Finally, the shift in composition of the age structure of the population, with marked increases at both ends of the age distribution, led to the expansion of government services to provide educational institutions for the young and housing and specialized services for the old.

Population growth, concentrated as it was in small and large urban centres, provided a ready market for industry, supplied the needed labour force, but also sharply increased the demand for public services.

Transformation of the Production Process

Both the general expansion of the economy and the urban explosion contributed to the transformation of the production process. The postwar era saw the full flowering of industrialism in Ontario. The war years had re-started the processes of urbanization and industrialization. In the postwar years these processes accelerated and rapidly changed the nature of Ontario's economy. The change, in the first instance, was from a predominantly primary goods orientation to a secondary manufacturing basis, and secondly, from a manufacturing base to a service-centered economy.

The speed of the maturing process was the dominant factor of the past twenty-five years. In that short period Ontario's economic base was virtually restructured. The obvious effect—decline in the relative proportion of people employed in agriculture and other primary industries—has tended to overshadow other significant developments. Among these are high rates of female participation in the labour force; general upgrading of employment in terms of intellectual and skill requirements; high rates of employment growth in service industries (including government).

The emergence in Ontario of a highly developed, diversified and mature industrial economy created social and economic problems that, in turn, put pressures on the government to become involved in the economic process. One contributing factor has been the concentration of economic development in a few regions of the province, particularly in the Metropolitan Toronto area and along the Macdonald-Cartier Highway 401 corridor. Most of Northern Ontario and large areas of Southern and Eastern Ontario were left out of the sweep of development and growth. This imbalance could be corrected only by government intervention either to ameliorate the problems or redirect patterns of industrial growth. Urbanization brought with it a host of problems, not the least of which was the provision of essential physical and social services.

These problems were not unique in Ontario. They were, and are, the by-products of the twin forces of industrialism and urbanization. The essential fact, however, is that in this process of change, Ontario, among the provinces of Canada, has been leading the way. The social, economic and political problems

that have emerged, are most intense in Ontario because Ontario is the first province to undergo the revolutionary shift to an urban-industrial society.

The Response of Government

An earlier publication of the Ontario Economic Council, "Ontario: A Society in Transition", explored the process of social and economic change in some detail. The arguments developed in that study need not be repeated. What we are interested in is the impact of all these developments on the political system, and in particular on the economic and fiscal policies of the Ontario Government. Economic growth, population growth and the transformation of the economy resulted in the massive intervention of government in all phases of Ontario's social and economic life. The involvement of government in handling the consequences of urbanism and industrialization led to the transformation of the government itself in terms of both its nature and role.

The only other comparable period of economic growth in Canadian history was the boom at the advent of the 20th century, from 1900 to 1913. The significant differences between this earlier period and the postwar era are matters of scale and intensity. In the 1900-1913 era, many immigrants coming into Canada settled on farms in the West. The economic impact, while substantial, did not have the same qualitative effect on production, because it operated within an economic framework created by Macdonald's National Policy. In other words, the 1900-1913 boom brought to fruition the plans, the technology and the infrastructure (primarily railways) that had been built up over the preceding quarter century.

The post-1945 era, on the other hand, brought with it far-reaching changes in transportation and communications, in patterns of living, in employment, in technology, and in industrial organization. It saw an orientation of Canada's exports from raw materials and food, to processed materials and manufactured goods. It is these qualitative differences that had an unprecedented impact on government.

The two central factors of the postwar boom were the dynamics of growth itself and the concentration of that growth in limited geographic areas, particularly large cities and the

numerous related smaller but sizeable cities. The twin process of urbanism and industrialization tended to put heavy pressure on the provinces and the municipalities to deliver the needed social infrastructure and services. Federal policy, although of vital importance, and contributing positively to growth, were peripheral to the main action and it was not nearly as involved in the building of roads, servicing industry, and planning and building communities.

The 1950's and 1960's saw the gradual but accelerating increase in the commitment of public funds and energies to solving the problems caused by economic growth, population increase and the changing structure of the economy.

Federal Economic Policies

The intellectual climate prevailing in Ottawa at the close of the war emphasized the overriding fear of a return to the conditions of the 1930's. The Advisory Committee on Reconstruction, reporting in 1944, forecast an immediate postwar boom followed by a rapid economic decline in 1952-54. The pessimistic outlook coloured federal thinking about the future economic prospects and reinforced the determination to introduce Keynesian policies to achieve economic stabilization.

Earlier, in 1941, the first step had been taken. The B.N.A. Act was amended to allow for the introduction of a federal unemployment insurance scheme. In 1944, the federal government introduced family allowances (baby bonus) as a built-in stabilizer. Finally, in 1945, the federal government issued the White Paper on Employment and Incomes—the official policy statement assigning the responsibility for achieving full employment to the federal government.

Two consequences flowed from this decision. First, the federal government took ultimate responsibility for the performance of the economy. This meant that the federal government was committed to intervene in the economy through fiscal and monetary measures. Its immigration policy and full employment policy meant that it had to maintain economic growth although economic growth was an implied rather than an explicit economic goal.

The second consideration was to establish the preeminence of the federal government in the area of economic policy. Given the tragic circumstances of the Thirties, and the virtual bankruptcy of many municipalities and several provinces, this position was understandable. The attitude of the federal government towards the provinces was revealed in the Dominion-Provincial conferences in the immediate post-war period. Initially, the provinces in general were not prepared to challenge federal leadership in economic matters, but there was little readiness to accept federal tutelage.

In retrospect, it may be seen that the thrust towards economic planning implied in the federal government's position and policies could not be maintained. Contributing to this was the defence of their constitutional powers by both Ontario and Quebec. But probably more important in the long-run was the misreading of the economic opportunities and pressures that triggered a post-war boom of unprecedented proportions. Events simply outstripped the plans of the economic advisers. Policies designed to mitigate the adverse effects of post-war reconstruction and prevent a recession had to be remodelled to meet the needs of expansion. The name of the game changed and the players were not prepared for such a dramatic shift of circumstances.

By the 1950's, the Korean War and the resource boom had radically altered Canada's economic outlook. In both cases, demand originated in Canada's close relationships with the United States. Federal economic policy had successfully shifted gears and a new series of initiatives had been launched in the mid-Fifties. High on the priority list were steps taken to move the newly discovered energy sources of the West to central Canadian markets. A new phase of the National Policy was evolving consisting of new transportation links across Canada (pipelines, air lines, the Seaway, and conversion of the railways to diesel) and new communication links (the microwave system); the gradual liberalization of trade through the medium of GATT; direct government support and expansion of the aircraft industry and the nationally owned air carrier; and the growing commitment to a nuclear energy program.

The recession years starting in 1957 barely blunted the emerging thrust of the new industrial Canada, and a change of govern-

ment in Ottawa was also a contributing factor to a shift in policy away from a centralist and economic perspective to a regional and social perspective. The combination of trading deficits, inflation, capital inflows, a high priced dollar, slow growth and high unemployment virtually defied solution. And the failure to realize any observable benefits from “the vision of the North” brought federal economic leadership into question.

Aside from spectacular wheat sales, the Canadian economy drifted until in the early Sixties a more favourable set of conditions pulled the economy out of the doldrums. The two key policy decisions underlying the resurgence of strength were devaluation of the Canadian dollar and the Canada-U.S. automobile production agreement. Beyond these crucial moves, however, the federal government tended to adopt an ad hoc approach to economic policy.

One of the features of the recession years was the debate between those who argued that the persistently high rate of unemployment was a structural problem and those who insisted that deficient demand was the problem. The resurgence of demand in the mid-Sixties and the decline in unemployment rates, settled the argument. But out of this debate came the focus on the need to develop manpower policies to improve the operation of labour markets.

Another area of activity in the early 60's was regional development: ARDA, ADA, The Atlantic Development Board and later in the decade, the Department of Regional Economic Expansion. The concern with and finally action on regional disparities added a new dimension to economic policy that involved government directly in business decisions.

Throughout the Sixties, government intervention in the private sector under the aegis of regional development, manpower or other economic policies led to an ever further involvement of government in business and this marked a decisive shift in relations between government and private industry.

The emergence in the mid-Sixties of a new series of policy questions (foreign ownership, competition policy, research and development, foreign trade, environmental deterioration) raised fundamental issues relating to Canadian economic and political relations with the United States. These issues raised sensitive

political problems and challenged the underlying assumptions upon which the whole postwar boom had been built.

By the end of the Sixties it appeared that the historic National Policy inherited from the 19th Century was no longer acceptable as the basis of federal economic policy; that economic growth was no longer acceptable as the sole criterion of the success of public policy; and that broader social and environmental issues must somehow be accommodated in economic policy. Given this situation, federal initiative economic policy was hamstrung by conflicting objectives and lack of a clear set of policy goals.

Summing up, the federal government's decision taken in 1945 to intervene in the economy to achieve full employment led to a situation where the government was now involved in all aspects of economic development, but without any clear and precise idea of the goals of economic policy. Instead of one policy we now had a bewildering array of policies, programs, agencies, advisory bodies and activities, some complementary and some contradictory. There was an obvious need to develop and to articulate an overall economic policy goal or set of goals that could be used as guidelines for economic policy. The goals set out by the Economic Council of Canada in 1963 were insufficient to accommodate many of the issues that have become relevant since that time.

Ontario Economic Policies

Clash of Economic Opinion

At the close of the war the prevailing opinion in Ontario on economic prospects contrasted sharply with federal thinking on two major counts. First, the provincial government looked forward to a period of rapid economic expansion. The mood of Ontario was captured by the Treasurer, the Honourable Leslie M. Frost, in his 1944 Budget address when he said:

“We are building not only for these times, we are planning for a greater population, for industrial expansion, for prosperous farms and for a happy and healthy people. We are laying the sure foundation for a greater and stronger Ontario.”

The second major concern of the provincial government was the provincial and municipal debt that had built up to record levels in the Thirties. The relative size of this debt may be grasped from the fact that one out of every five dollars of provincial revenue was required for debt servicing. The plight of the municipalities was also of prime importance, and the key plank in the Conservative platform for the 1943 election was the

promise to reform the municipal tax system and reduce the burden of real property taxation.

Ontario remained committed to the concept of balanced budgets. In fact, however, the balanced budget in the immediate postwar years included a surplus used for debt reduction. (The net debt was reduced in 1945, 1946 and 1948).

The Aim Was Expansion

Provincial economic policy in the late 1940's was geared to industrial expansion. This was reflected directly in programs of the newly created Department of Planning and Development, designed to coordinate government activities and to promote industrial growth. This new department was particularly concerned with assisting existing industries to expand their operations and the attracting of new industries to the province. The government discouraged "cut-throat" competition among municipalities to attract new industries through business and property tax-concessions. It set up a division that provided detailed information on all potential sites for industry. It attempted to work with municipalities to ensure a degree of industrial decentralization in Ontario.

Labour legislation governing industrial disputes, certification of unions and protection of employees was brought into force during the war with the passage of the Labour Relations Act, The Rights of Labour Act and The Hours of Work and Vacations With Pay Act. These Acts, together with the existing Industrial Standards Act, apprenticeship and safety legislation formed the basis of labour policy in Ontario until the 1960's. On the whole, the legislation was progressive in intent and reflected a recognition of the role of organized labour in an industrial society.

Ontario policy with respect to resources stressed exploitation with a limited, although growing, concern with conservation and proper management of renewable resources. The resource departments were still considered to be revenue generators. One constant thread of resource policy was the continuing desire to ensure the further processing of raw materials in the province. To this end the Mining Act had been amended in 1917 and a ban on the export of pulp wood was introduced in the 1900's.

All of this effort was directed towards the creation of a proper climate for economic development. The government and people were well aware of the need for a favourable political environment to attract investment capital. Working on the assumption that the province's geographic location with respect to raw materials, markets and labour supply gave it an advantage over other areas of Canada, the provincial government endeavoured to provide the most attractive political climate by stressing sound financial policies (i.e. balanced budgets and low taxation).

Building a climate of confidence was not enough. The government was faced with two pressing problems as Ontario emerged from the war years: The existence of both 60 and 25 cycle electrical systems in the province, and the backlog of public works—roads, hospitals, water and sewage works, rural electrification, schools—that had built up in the depression and war years. These required direct or indirect provincial expenditures on an unprecedented scale. The underlying problem of fiscal policy in the postwar years in Ontario was the need to accommodate a huge government capital investment program and at the same time maintain a climate favourable to private investment for the creation of jobs in developing urban areas.

The Drive for Industrial Expansion

There is no question that the province's commitment to industrial expansion undertaken in 1944, was more appropriate to the postwar era than was the federal government's concern with a possible recession. This conflict in expectations is the root of discord in the Dominion-Provincial Conferences in the postwar period.

By the early 1950's the federal policy stance shifted to emphasize national economic development and that this complemented and reinforced Ontario provincial policies. An era of accommodation was achieved and both the provincial and federal governments, operating primarily within their own jurisdictional fields, cooperated on major projects such as the gas pipeline, the Seaway and the Trans-Canada Highway. In addition, federal funds for housing, land assembly, hospitals and other public works supplemented provincial programs. The growing spirit of cooperation and mutual support also led to a

series of shared-cost agreements on highway construction and welfare. Then in the late 50's the historic hospital insurance scheme was signed. The basis for an explosion of shared-cost programs in the 1960's was established.

From Ontario's viewpoint, although the 1950's was a period of general expansion, three new problems emerged that led to changes in economic policy; the slowdown in the growth of employment in manufacturing; a concentration of population and employment in large urban centres; the decline of agriculture and the squeeze on farm incomes.

At the beginning of the 1950's, Ontario's economic policy was straightforward: The encouragement of economic growth and industrial expansion. By the end of the 1950's, slower growth and higher unemployment were complicated by a new set of structural problems that required new policy responses.

As early as 1953 the province was becoming aware of the imbalance of industrial development and the resulting growth of severe pressures on housing and land costs in the Toronto area. Although decentralization of industry was a stated objective of the Department of Planning and Development, there were neither positive incentives nor restrictive measures introduced to influence plant location decisions. The department provided advice and statistical data, but tended to let market forces determine site choice. Inevitably this led to a concentration in southern Ontario, particularly in what came to be known as the "Golden Horseshoe" around the western end of Lake Ontario. In 1954, to encourage a greater degree of industrial decentralization, a regional development program was introduced.

At the same time, the province created the Municipality of Metropolitan Toronto. The success of this venture in municipal reform in solving the water, sewage, transportation and housing problems in the Metro area created a powerful counter-pull to industry that had begun to look to other areas of the province. The failure of the original regional development program stems in part from the establishment of Metro, which rapidly became a magnet for immigrants, for migrants from other parts of Canada, and for industrial development.

A Shift to Service Industries

Another source of the problem was the slowdown in investment in manufacturing and, more importantly, the virtually stagna-

tion in manufacturing employment through the whole of the 50's. Employment increases in the decade were more rapid in the service sector. A rising proportion of women was entering the labour force, taking jobs in the service industries.

Provincial policies geared to industrial expansion (and this meant secondary manufacturing) were inappropriate to an economy shifting from goods to service industries. This transformation, even when acknowledged, was seen as somehow peripheral to the real need for the expansion of secondary manufacturing. As a result, there was a failure to encourage and assist service industries that were the primary source of jobs. The major exception to this rule, of course, was the expansion of employment in the public sector itself, including education.

Finally, the problems facing farmers required urgent action and the province originated a series of programs to increase productivity, extend credit and introduce forms of supply management through marketing boards. The central problem appeared to be too many producers, a problem not to be tackled head-on. The government tried to find methods of satisfying conflicting social, cultural and economic objectives.

By the early Sixties a whole new set of remedies to the problems of slow growth and unemployment began to emerge. These can be classified as (a) stop-gap programs—winter works, roads to resources (both federal-provincial); (b) industrial development programs—import replacement, overseas sales missions, attraction of investment and financial assistance to industry (all provincial programs) and (c) long-term programs—vocational and technical training, manpower training (federal-provincial).

New Relation with Government

The growth of structural policies (as opposed to the traditional fiscal and monetary policies) brought government and industry into a new relationship. No longer was the government, federal or provincial, an interested bystander in the production process, it was involved in and influenced all manner of business decisions.

This new approach to economic policy was reflected in labour policy. In the 1960's, for example, the Department of Labour became directly involved in a series of programs relating to

human rights, women's position in the labour force, the development of skilled manpower, the improvement of the apprenticeship program, minimum wages, improved safety and industrial standards. The thrust of activity, legislation, regulations and involvement was a positive response to the changing structure of the economy.

Unfortunately, however, in this outburst of creative enthusiasm, the problems of industrial relations, particularly as they related to a changing economy and technology, were not resolved. Though much was said about improving the system of collective bargaining, little was accomplished. The government appeared to favor legislation to resolve problems that might have been handled within the collective bargaining framework.

Outstanding among the developing issues was the question of collective bargaining in the public sector and the right to strike. In this area government policy vacillated. Although full collective bargaining rights were achieved by municipal employees, they were not granted to provincial employees, and compulsory arbitration was imposed on hospital workers. The failure to come up with a consistent policy and to demarcate "essential services" left a serious and growing problem festering in labour relations in the province.

A marked shift in economic policy took place in the early Sixties with the development of a series of industrial expansion programs. Under the general banner of the "Trade Crusade", the province introduced programs to help Canadian industry expand output and sales in domestic and foreign markets. Included was the opening of trade offices in the United States and abroad. An important part of the overall policy was the encouragement of foreign industries to establish branch plants in Ontario. Other programs included assistance in arranging for joint ventures and licensing agreements.

A new feature was the establishment of the Ontario Development Agency. Originally set up to provide advice to small companies and to guarantee loans from conventional lenders, it soon changed to a corporation with power to make loans. In 1967, the ODC introduced the Euqualization of Industrial Opportunities program that consisted of forgivable loans to companies locating in selected areas. For the first time the province used incentives to influence location decisions.

A similar evolution was apparent in housing with the change in status of the Housing Branch to the Ontario Housing Corporation. After the amendment of the National Housing Act in 1964, the OHC rapidly emerged as the sole supplier of low-income housing and took over responsibility for management of existing subsidized housing from the municipalities.

The creation of the Ontario Water Resources Commission in 1957 to assist municipalities to build water and sewerage systems also evolved steadily. By the mid-sixties OWRC was building systems and charging users on a fee for service basis. The construction of appropriate water systems was essential for industrial development in cities not located on the shores of the Great Lakes. In 1965 all new industries or major expansions to existing industries were required to obtain approval on standards for waste disposal into watersheds.

Regional Industrialization

In 1966, the province announced its new regional development program. Implicit in the program was a greater equalization of industrial development in less favoured regions based on the human and natural resources available.

A central feature of the new regional program was the recognition that provincial expenditures were sufficient to influence development in the various regions of the province. And the province announced that henceforth these regional effects would be considered in the thrust of its budget. To achieve co-ordination of action a Cabinet Committee and a Deputy Minister's Committee were established.

The importance of economic growth was also recognized in the development of educational policy. The rapid rise in expenditures, first on secondary schools and then on post-secondary schools—both universities and Colleges of Applied Arts and Technology—was justified under the rubric of “investment in human resources”. For example, the following statements can be found in the budgets of the period:

“The Province’s expenditures on education represent a substantial investment on behalf of our young people, an investment that will bring invaluable returns in future years.”
(1963)

“There has been an enormous rise in expenditures on education, job training and health. Such relatively intangible assets are essential if we are to improve the efficiency of labour and if we are to make the scientific and technological advances necessary to keep us internationally competitive.” (1964)

“In this fast-moving technological age, education represents an essential investment of great economic consequence. This economic fact is exercising a marked influence on the educational program.” (1966)

The Budget Becomes Instrument of Growth

The series of initiatives taken in economic policy development came to a head in 1966 when, in addition to the announcement on regional development (Design for Development), the provincial budget spelled out the new role of government:

“ . . . the steady growth of government expenditures has broadened the direct impact of government on the economy and made the provincial budget a delicate instrument of economic and fiscal policy . . . the provincial budget contributes directly to the character of aggregate demand in the provincial economy and to the economic productiveness of our people and institutions . . . ”

The Treasurer went on to outline four principles of economic policy:

1. The establishment of expenditure priorities on the basis of their contribution to growth and productivity.
2. The introduction of long-range planning.
3. The coordination of all policies and programs within the long-range plan.
4. Coordination with federal and municipal governments.

The essential features of this statement, particularly when combined with the new regional development policy, are the full acceptance of fiscal policy as an instrument of economic policy, and its use by the province for provincial purposes; the establishment of economic growth as the central objective of economic policy; and the establishment of economic planning as a policy principle.

The 1966 budget statement marked the full acceptance of the province's role in contributing to provincial economic growth. Until then, the province had recognized the prior responsibility of the federal government in economic policy. Given a national position, the province had adjusted its spending and revenue programs to accommodate federal initiatives. For example, Ontario had always adjusted its corporation tax to accord with federal legislation.

After 1966, however, a new approach to fiscal autonomy was enunciated. In an earlier period, the Honourable Leslie M. Frost had set out the relationship between the province and the federal authorities in these words:

“The primary responsibility for maintaining high levels of income and employment lies, of course, with the federal government . . .

“In partnership with the federal government the provinces and the municipalities may, nonetheless, make an extremely important contribution to economic stability by undertaking a program of useful capital works.” (1955)

Compare the tone of this statement with the following quotation from the 1971 budget:

“In early 1970 and again in last year's budget, the Ontario Government warned the federal government that the single purpose thrust of its policies to reduce inflation would create unacceptably high levels of unemployment throughout Canada . . . The Ontario Government did not agree a year ago, and does not agree now, that this deliberate federal policy of high unemployment is a sound and just way to fight inflation.”

The emergence of a fiscal policy component to the province's overall economic policy greatly expanded the range and scope of economic policy. This development is crucial to an understanding of the emergence of economic policy in Ontario.

The 1966 budget statement did not solve all the problems of coordination of economic policy, it pointed the way to the future. To accomplish the degree of coordination required, there

was a need for major reforms in the structure of government in Ontario. Three main thrusts of reform were introduced:

1. The reorganization of municipal government. (Design for Development, Phase II and Phase III, Municipal Tax Reform).
2. The revamping of the regional development program. (Design for Development, Phase II and Phase III, Design for Development: The Toronto-Centered Region).
3. The restructuring of the provincial government. (Committee on Government Productivity).

Reform in Policy Making

The period from 1946 to the 1970's was one in which the energies of the provincial government were directed towards the reform of the policy making and policy implementing structures of government, including the municipal system. This process was not made any easier by the shift in the goals away from the narrow pursuit of economic growth and industrial expansion. Two central facts should be noted:

First, the province's position on its role in economic development changed. In the first two decades of the postwar era the province's economic policy was limited to the creation of the appropriate climate for private investment. This attitude was best expressed by the 1958 budget.

The explosive growth of provincial expenditures, particularly after the introduction of hospital insurance and the massive infusion of funds into education changed the relative position of the province in terms of its influence on overall economic conditions. This was recognized and became the theme of the budgets after 1966. The 1969 budget, for example, contains the following statement:

“A modern budget is not simply a bookkeeping statement or a testimony to financial management. It is a deliberate instrument of social and economic guidance; it is part of the very fabric of our society and economy.”

By the beginning of the 70's, then, the province had evolved a new approach to economic policy, one which stressed the crucial role of the province itself and its expenditure and revenue decisions.

Second, the nature of the problem that government increasingly was called upon to deal with had changed. The essence of the new imperative was usually expressed in the phrase “quality of life”. It was no longer enough to provide essential services and to facilitate the process of economic growth. Economic growth, although desirable, was hedged in by new concerns relating to the protection of the environment, human and civil rights, involvement in the planning system, the shift from car to public transit. This new attitude was most clearly expressed in the anti-development stance of reform councils in urban municipalities.

Summing up, the evolution of economic policy in Ontario saw a marked shift from a policy of response to need to a policy of shaping growth. Having committed the province to a position of leadership in the pursuit of economic growth and having begun the process of reforming the institutions of government to meet this challenge, a change in attitudes towards growth itself raised the whole question of the purpose and role of government. This fundamental shift in the rules of the game has erected tensions that the system was not, as yet, equipped to deal with. The requirements for the decade ahead in terms of economic policy were not clear.

Fiscal Policy

The provincial government approach to fiscal policy in the immediate postwar years was far more orthodox than that of the federal government. Senior federal officials were convinced converts to a Keynesian approach, seeing fiscal policy as a tool for economic stabilization. The province continued to espouse the virtues of a balanced budget.

It would be a mistake, however, to dismiss provincial financial policies as having no direct bearing on economic policy considerations. Two factors should be noted. The province was constrained by the wartime tax-rental agreement; and the Treasurer of Ontario was vitally concerned with the debt position of the province and the municipalities.

Guardian of the Province's Credit

In his budget address of 1944, Mr. Frost gave a comprehensive statement of the province's debt position and at the same time outlined a general debt retirement plan that might be adopted on the termination of the wartime tax agreement. The plan was to retire annually a certain amount of the existing debt out of surplus revenues and to repay new debt on a serial basis within the life of the works for which the debt had been created.

In 1946 Mr. Frost announced a surplus on ordinary account, a reduction in Gross Debt and a reduction in Net Debt, emphasizing that this was the third year in succession in which a reduction in Net Debt had been achieved due to prudent management. The significance of this achievement, he pointed out, was that the strong financial position of the province was reflected in its high credit standing and the resulting low rates of interest at which the province was able to borrow.

The financial policy to be followed was based on the belief that a balanced budget would conserve the Government's credit for later development expenditure. The balance, he said, should be achieved without the imposition of new taxes while, at the same time, the Public Debt should be reduced. It was a pay-as-you-go policy, holding in reserve the provincial credit for use in conditions of emergency and when expansion became possible.

In his budget address of 1947, Mr. Frost drew attention to three accomplishments of the years 1943-1947 which he maintained were an impressive demonstration of the soundness of the fiscal policies of the provincial government: the reduction of the Net Debt by \$2,025,716; the addition to investment in the Provincial Highway System of \$2,980,804; and the widening of the scope of benefit for developmental services—Agriculture, Education, Health and Welfare—by the spending of \$231,045,373.

In a period of general economic expansion and rising revenues, the Frost strategy was to use the revenues generated by the existing tax system to pay for "ordinary" expenditures and to finance "capital" expenditures in part from revenues and in part by borrowing. Overall, the government's objective was to cover ordinary expenditures with current revenues and finance as large a portion as possible of capital expenditures on a pay-as-you-go basis.

The key to the budgetary system was the division between ordinary (current) and capital expenditures. The province kept two sets of books. Each year the financial statement was adjusted to show a modest "surplus" on ordinary account, with a deficit on capital account. Excess revenues were transferred to "The Highway Construction Account" which was used to finance capital projects.

The financial policy of the government in these early years was directed primarily at the goal of reducing the level of debt and thus achieving a favourable credit rating. The revenue from the tax-rental agreement was sufficient to accomplish this end and at the same time provide for a rapid rise in expenditures. The annual average increase in provincial net general expenditures (including both current and capital) exceeded 24 per cent between 1945 and 1948. Net general expenditures rose from 3.6 per cent to 4.7 per cent of personal incomes in the province.

The Aim was Debt Reduction

It is interesting to note that in 1945 it required 21.6 per cent of provincial government revenues to meet the cost of debt servicing. In 1945-46 \$600,000 was saved in interest and foreign exchange, and consequently only 19.1 per cent of provincial government revenue was required to meet debt servicing in 1946. This percentage dropped to 15.1 per cent in 1947 and 11.3 per cent in 1948 following a reduction of over \$27 million in the provincial net debt during 1947-48. It subsequently rose again slightly to 13.6 per cent in 1949 and 13.8 per cent in 1950. In the 1945 fiscal year, net debt per capita stood at \$120.86, 13 per cent of personal income per capita. In 1965 net debt per capita stood at \$200.25, 8 per cent of personal income per capita. By 1971 the figures were \$196.14 and 5 per cent respectively.

The stress on debt reduction was part of a broader scheme of financial policy. Frost clearly recognized the emerging commitment to vast outlays for the building of physical assets. His position was best expressed in the 1948 budget:

“Since we have assumed office we have endeavoured to finance the advances of the future out of the savings achieved by better management . . . Now we are accumulating against our capital commitments for highways and various public works with the object of keeping our net debt completely in hand . . . Net debt must be paid from taxation. Interest and principal constitute a first charge on our revenues.”

The other side of the coin, of course, was the revenue situation. Until 1947, the province operated within the limits imposed by the tax-rental agreements. Revenues from the major direct tax fields (personal income, corporation income and succession

duties) were under the control of the federal government. The province looked forward to the withdrawal of the federal government from these key tax areas at the conclusion of the war-time agreement.

The position taken by Ottawa, as announced at the 1945 Dominion-Provincial Conference on Reconstruction, was totally unacceptable to Ontario. The province wanted access to the growth taxes to finance its planned expansion of capital spending. The federal promise of massive financial assistance in health and welfare was not acceptable to a province that had worked out its own spending priorities.

The reaction in Ontario was predictable, and the Treasurer spelt out the province's position in strong terms. In the 1947 budget he insisted that the province must have fiscal autonomy.

“In a federal system,” he said, “such as we have in Canada, the central authority and the provinces should have, as far as possible not only different heads of revenue but also different heads of expenditures. Provinces cannot retain their fiscal autonomy and function with maximum efficiency if they have to depend upon the federal government for contributions and subsidies. The tendency would be for the provinces to become extravagant and subservient to the central authority.”

Subsequent experience such as the extravagance of educational spending in the Sixties and the subservience of the province in Medicare, has confirmed the forebodings of the Treasurer of Ontario. In the same budget address he reiterated the determination of the province not to endanger its development by permitting excessive centralization of powers with the federal government.

“We do not intend”, he said, “to undermine the strength of our province or of Confederation by consenting to the centralization of powers which will leave the development of our great heritage in other hands. We do not ask any other authority to do our job for us.

“The assignment of our rights in the direct tax fields on the basis of the Dominion proposals would, within measurable time, place Ontario in a restricted and limited financial posi-

tion which would shortly leave the development of this province, if such a development were to take place, in the hands of a central government.”

The demand for fiscal autonomy was an outgrowth of the divergence in views between Queen’s Park and Ottawa on the appropriate policies to be followed in the future. Ontario stressed the need for the expansion of a social and economic infrastructure to meet needs arising from industrialization. Ottawa was concerned with providing better social services and preventing a recession. Conflict over taxing powers endured through the years. The demand for fiscal autonomy appeared again in the budget speech of 1971.

During the Fifties and Sixties, a general agreement on the priority of economic growth created conditions for an accommodation on fiscal matters, even though the province was never fully satisfied with the tax agreements. Given this shared outlook, Mr. Frost’s warning about the dangers inherent in shared-cost programs was conveniently forgotten.

The essential fiscal policy problem at this time was seen as the cultivation of a climate for growth through the implementation of sound financial policies, that is, low taxation and a restriction upon the accumulation of debt. In this way, it was felt that fiscal policy would contribute indirectly to the expansion of industry. Fiscal policy, therefore, was an element, although a passive element, of an economic policy designed to stimulate economic growth in Ontario.

It was in the 1948 budget address that Mr. Frost was able to announce that spending on the expansion of the province, as planned and anticipated, could proceed. In the four-year period ahead up to 1952, in addition to \$20 million for refunding maturing old debt, \$350 million of new money was required for developmental projects. These projects, particularly those related to Ontario Hydro, were to be self-liquidating and therefore not a cost to the taxpayers as such. The financing was to be achieved by the use of the province’s credit in the form of guarantees to enable subsidiary bodies to borrow the money which would then be repaid from the income of the works created.

In furtherance of the policy of fiscal autonomy stated in 1947, from 1947-49 the province had refrained from re-entering the personal income tax field and had not signed the 1947-52 Dominion-Provincial Tax Agreement. And, in 1947, the province decided, in addition to not levying a personal income tax, not even to require the Federal Government to pay any sum in lieu. But by 1950 the situation had altered. Very large works projects could not be postponed much longer. It was decided to claim the 5 per cent of taxes paid by Ontario taxpayers to the Federal authorities and to apply the money received to the Sinking Fund provisions for debt retirement. This would keep the province's credit position strong.

1950-1957: Fiscal Policy on Capital Spending

The financial policy followed in the 1950-57 period, as in the post-1945 era, was to cover ordinary expenditures with current revenues and finance as large a portion as possible of capital expenditures on a pay-as-you-go basis. But the Honourable Leslie M. Frost was not loath to borrow for capital purposes and he now added the clearly expressed policy intention to use such borrowing and capital works to deal with unemployment:

“If we run into any substantial volume of unemployment, we would be expected to play an active part in financing an expanded public works program without increasing taxation. In such a period, we would resort more extensively to financing our capital program by using our credit . . . ”

This statement reflected the dominant concept of contra-cyclical policy evolved at that time. Frost considered the role of the provincial government and of the municipalities in economic policy to be limited. Insofar as the province played a contra-cyclical role in the economy, the major weapon was expenditure on capital projects. For example, the public investment program projected for the fiscal year 1955-56, was directed, specifically, to the alleviation of unemployment.

Capital spending was, however, more than a device to stimulate employment. The fiscal policy of the Frost era centered on provincial government expenditures for capital projects, both as a device to stimulate employment in periods of economic slack and as a positive instrument of economic growth. The provincial government recognized the central role of the province and the municipalities as provider of essential services.

The concept of the province's fiscal policy emerged over time. As in the post-1945 era, in the early Fifties the budgets stressed the importance of the soundness of "financial administration". The 1952 budget, for example, contained an elaborate rationalization of an increase in the net debt of the province, without reference to fiscal objectives derived from spending on capital projects.

By 1953 a change in approach to capital spending was beginning and the budget's tone shifted to a mood of growth and expansion. It was a developmental budget and was deliberately directed towards industrial expansion and the creation of new employment opportunities.

In 1955 the budget began to focus on the relationship between government spending and the stimulation of general economic activity. But it was the 1956 budget which was crucial in the development of fiscal policy in Ontario. For the first time, spending on capital projects was seen as essential to economic development.

The stress placed on the importance of capital projects in the 1950-57 period was reflected in the percentage distribution of net expenditures by functional classification. In 1950, highways accounted for some 25 per cent of total net provincial expenditures. This increased to 33.4 per cent by 1957. Spending on public works rose from 3.2 per cent to 6 per cent. Education remained at 19.1 per cent of total net expenditures and Health, Welfare, Law Enforcement and Reform, and Resources were reduced slightly.

The overall strategy of the province, the creation of a desirable investment climate through low taxation and limited increase in debt was possible as long as expenditures did not run ahead of revenues. The shift in approach from debt reduction to the prudent use of provincial credit to borrow for capital projects announced in 1948 was feasible only up to a point. Hydro borrowing, although guaranteed by the province, was not reflected in net debt. Thus Hydro could carry out substantial capital programs without seriously limiting the capacity of the province to borrow.

But the major constraint to provincial spending was a limitation of resources. In order to maintain taxes at a low level, expendi-

tures had to be maintained in line with the growth of the economy as a whole. Net provincial expenditures as a percentage of personal income in Ontario remained relatively constant, ranging between 5.2 and 5.7 per cent between 1948 and 1954.

In 1955 capital spending became a conscious contra-cyclical device. An announcement made in 1956 asserted that capital spending was essential to growth. This created an entirely new provincial fiscal stance. From this point on the low taxation policy had to be abandoned in a wave of increasing spending commitments. Between 1954 and 1957, net provincial expenditures increased as a percentage of personal incomes from 5.6 to 6.6 per cent.

The Search for Revenue: 1957-1962

As the Ontario government saw it, the revenue difficulties of the province, as well as of the municipalities, sprang in part at least from the exigencies of World War II and the Federal-Provincial fiscal arrangements that emerged from it. During the war the rates of direct taxation imposed by the Government of Canada were raised to extraordinarily high levels to meet the conditions of total war. At its termination this left the Federal Government deeply entrenched in the main direct tax fields to which the provinces are confined by the constitution. Although from time to time adjustments had been made in these rates to provide a larger area of taxation for the provinces, in 1961 they occupied only one-fifth of the total corporation income tax field and one-seventh of the personal income tax field.

In 1945, net provincial government expenditure had amounted to \$132.3 million. In 1950 this had reached \$305.4 million and, in 1957, \$671.3 million. From 1957 to 1962 the average annual increase in net provincial government expenditures was 10.5 per cent until the total reached \$1,106.5 million in the 1962 budget.

In the thirteen years prior to 1957, nearly two-thirds of the province's capital projects amounting to \$826 million of new physical assets had been financed out of current revenue. But the province's capital program had recently been so large that an increasing proportion of it had had to be financed by borrowing. During this same period Ontario's population had increased by 1,500,000 while \$20 billion had been invested

in its factories, commercial buildings, new machinery and equipment, natural resources, housing and other capital assets. To the Ontario Government and the municipalities fell the responsibility of providing those essential services of education, highways and roads, hospitals, water and sewerage works, conservation, and development projects, without which urban development could not occur, nor industry flourish. On them, in addition, devolved a major part of the task of maintaining an economic environment friendly to industrial expansion and to the creation of new employment opportunities. The swift advance of Ontario's economy necessitated a huge expansion in all these services and the problem was intensified in many of these fields by the existence of a heavy backlog of need inherited from the depression and the war years.

In his 1948 budget address, referring to his budget addresses of 1943 and 1944, the Honourable Leslie M. Frost had spoken of progress in the declared policy of making a sweeping revision of the whole system of real estate taxation and also of increased municipal expenditures which, he hoped, had now reached their peak and would from then on tend to recede: He concluded:

“ . . . the upward trend of municipal costs is at a point of stabilization and from now on we may look to municipal reductions.”

But by 1957 demands for highways, schools, hospitals and other projects, and the pressures to give financial assistance to the municipalities, had confronted the province with a massive capital investment program.

By 1962-63 the municipalities, schools boards and other local agencies were receiving \$454 million from the province. This represented over 45 per cent of the province's total revenues as compared with only 18 per cent 20 years previously.

Pressures on the expenditure side were creating unprecedented demands on the provincial revenue base. There were only two avenues open to the province. Either it could get a better deal from Ottawa under the tax rental system (the province had signed an agreement in 1952), or it could use its own taxing powers. Until the province knew what the federal offer would be it could only wait and see.

As the tax rental agreement of 1952-56 was running out, the Federal Government fixed tax abatements for the new agreement at 10 per cent of the federal personal income tax collection at 1956 rates, 9 percentage points of corporation income, and 50 per cent of federal succession duty collections in the province. Ontario had made it plain that the minimum formula required was 15:15:50.

In November, 1957, following the election of the Diefenbaker government a new Federal-Provincial Conference was convened and the attitude of the federal government was considered to be cordial and receptive. A particular benefit achieved by the province was a change in the method of sharing the cost of unemployment relief assistance. Another achievement of the November conference related to hospital insurance and permitted the Ontario Hospital Services Commission to go ahead with its plans to bring the Ontario program into operation on January 1, 1959. The federal government also doubled its capital grants for hospital construction. Still another advance was the amendment to the Tax-Sharing Arrangements Act, which for the year 1958 increased from 10 to 13 per cent the standard rate of individual income tax. The province regarded this as an interim arrangement on the way to its proposed formula of 15:15:50. Virtually all the revenue to be obtained from the three major direct tax fields was to be paid over to the municipalities, the school boards and other local agencies.

The Ontario budget address of 1959 welcomed the federal government's proposal that the entire subject of financial relations with the provinces be re-examined, using the machinery of the existing Federal-Provincial Continuing Committee on Fiscal and Economic Matters. Federal-Provincial conditional grants and shared cost programs were considered by the province to be needlessly complex, creating many time-consuming and costly administrative difficulties. And on tax-sharing arrangements the Treasurer said that there had been no change in the province's position. The province did not believe that the existing distribution of the two major direct fields of taxation was just and equitable to the province. The province had never failed to stress the need for a revision of the arrangements.

In 1961, after reviewing tax-sharing since World War II and the 1945-46 Conferences, the Ontario Treasurer reiterated the right

of the province to a 50 per cent occupation of the fields of personal income tax, corporation tax and succession duties, but agreed, as a compromise, to a formula of 15:15:50. The new proposals for the five-year period April 1, 1962 to March 31, 1967 as advanced by the Government of Canada at the Federal-Provincial Conference of February, 1961 afforded some improvement, but fell short of meeting the province's revenue requirements. The Treasurer introduced the first provincial retail sales tax. And in 1962 a considerable portion of his budget address was devoted to justifying the retail sales tax which he still found necessary although there had been an increase in the federal income tax transfer from 14 per cent to 16 per cent.

Another Revenue Source: Shared-Cost Programs

Prior to 1957, federal grants had been important in several areas for many years. A whole series of grants supported provincial welfare services (the so-called categorical assistance programs), housing, and the Trans-Canada highway. But hospital insurance was a major turning point in federal-provincial financial arrangements. Henceforth, at least for the decade of the Sixties, provincial expenditures on health, education, housing and welfare, the key priority items, were to be closely bound to federal programs. Ontario was entering upon a new phase in the development of federal-provincial relations.

The first budget brought in by Hon. James Allen, in 1959, is of particular importance in that it marked the beginning of hospital insurance. Although the details of the hospital insurance scheme had been hammered out in a series of federal-provincial conferences going back to 1955, the agreement marked the first massive infusion of federal funds into an area of provincial constitutional jurisdiction.

Also in 1959, in the urban field, the province joined with the federal government in defraying 75 per cent of the cost of acquiring and clearing land for public housing redevelopment projects. The federal "Roads to Resources" program led to another new agreement. The change taking place was a subtle shift from programs initiated by the province and paid for out of provincial revenues, to a series of programs partially financed federally and reflecting federal initiatives. Ontario's industrial

development was a considerable factor in increases in revenues collected by the federal government, and the province was entitled to share in them.

In 1961 a new agreement was signed—the Federal-Provincial Technical and Vocational Training Agreement. It was made necessary in part by the educational needs of immigrants admitted to the country by federal initiative. This agreement coincided with a series of education reforms including the Robarts Plan, the expansion of trade schools, the Tax Foundation Plan and the increased financial support to universities. But, again, one key to the rapid growth in educational spending was the availability of federal funds.

The incursion of federal cost-sharing programs into the fields traditionally associated with provincial policy (resource development, health, education and welfare) was not resisted by the provincial government. For the most part, the federal initiatives fitted into the provincial priorities. And, more importantly, the additional funds were absolutely necessary, given the relatively narrow provincial revenue base. Although there were rumblings of discontent about the impact of the cost-sharing approach, the province did not raise serious objections to the trend in federal-provincial financial arrangements. The province committed itself to long-term expenditure programs that depended on the continuation of federal financial support.

The Emergence of Fiscal Policy

The recovery of the economy in 1962 and the boom conditions of the next seven years totally changed the revenue position of the province. The new tax-sharing agreement signed in 1962 and the existence of massive federal funds under a host of shared-cost programs provided the revenue base for an explosive growth in expenditures.

Between 1963 and 1969, net provincial general expenditures rose at an annual average rate of 16.8 per cent. The provincial budget tripled in seven years. The significant change in spending, from the Fifties, was the shift from massive capital investment to current spending.

About fifty cents of every dollar of provincial revenue was earmarked for transfer to municipalities, school boards and other

local government agencies under conditional and unconditional grants. Much of this went into capital works. But the important point is that the province no longer saw the wisdom of breaking down expenditures between capital and current spending. By 1968, the province dropped the separate current and capital accounts system and introduced a new consolidated system—net general and gross general expenditures. The difference between these two was the grants accruing to the province under the shared-cost programs.

The decision to move to a net general expenditure base (used first in the Smith Committee Report of 1967) was also a reflection of the new fiscal policy approach of the government. As provincial spending moved up to over 10 per cent of personal income, and as combined provincial and municipal spending surpassed federal spending in the province, the province saw its total expenditure programs as a major economic policy lever.

In 1967 the Honourable Charles MacNaughton introduced a combination budget statement and Budget Papers as a first step in a new format which, he said, reflected the substantially changed position of the provincial government in the economic and financial life of the country. Enlarging on this he said:

“The budget itself is a delicate instrument of economic and fiscal policy which has a profound influence on the character, direction and extent of economic growth and on the financial markets of the country . . . As a reflection of determination to proceed purposefully towards overall short-term and long-term goals of an economic and financial nature, the Government has established the necessary machinery to coordinate all matters relating to fiscal, budgetary, economic and inter-governmental policy.”

He explained that the analysis into the whole provincial economy which was now possible provided guidance on “. . . the effect of our fiscal policy in terms of the total budgetary impact upon the economy.” This policy found its strongest expression in the budget address of 1969 and the Budget Paper accompanying it:

“The Ontario Government intends to establish its own personal income tax system within the next two years. This

move to an independent income tax is necessary to preserve the Province's fiscal integrity and to achieve meaningful tax reform in Ontario''

This statement of fiscal integrity as a principle of the new fiscal and economic policy of Ontario brought the story full circle. The province's insistence on fiscal autonomy in 1947 had been a reflection of basic disagreement between Ottawa and Queen's Park on the future economic and social development of Canada and Ontario. The accommodation of the Fifties and Sixties and the growth of the massive shared-cost programs, equally reflected a basic agreement on priorities and goals.

By the end of the Sixties, however, a divergence of opinion was developing. The province objected to the federal government's insistence on moving ahead with the medicare scheme. It distrusted the motives of the federal government's decision to cancel the Vocational and Technical Training Agreement and replace it with a new manpower training scheme. It saw the unilateral federal tax reform move as a centralizing device that completely ignored the findings of the Tax Structure Committee. And finally, it was concerned that federal economic policy was designed to limit the potential economic growth of Ontario under the guise of regional economic development.

In no small measure, the move to articulate a separate and distinct provincial fiscal policy was a reaction to federal policies that were seen as detrimental to Ontario.

The Increase in Provincial Government Expenditures

In 1945 (the 1945-46 fiscal year) net general expenditures stood at \$132.2 million. Twenty-six years later, in 1971, provincial net expenditures reached \$4,262.5 million, more than 32 times the 1945 level. (See Tables I, II, III and IV following.)

This increase in expenditures reflected price changes as well as real growth. Using the implicit price deflator for government expenditures on goods and services (1961 = 100), an estimate of the increase in net government expenditures in constant dollar terms could be calculated. On this basis, provincial government spending increased from \$291.4 million in 1945 to \$2,497.1 million in 1971 or by 8.6 times. On an annual percentage basis, inflation accounted for 5.1 per cent of the yearly increase in expenditures.

This rate of price increase compared very unfavourably to price movements in the economy as a whole. Whereas the implicit price index for government expenditures on goods and services rose by 276 per cent between 1945 and 1971, the implicit price index for Gross National Expenditure increased by 145 per cent.

Although productivity measures (output per man-hour or output per person employed) are suspect when applied to services, they do give some indication of relative performance. Unfortunately, aggregate productivity rates are not available for the non-commercial service sector (including public administration and defence). The data for commercial service industries, however, show that their productivity rates are substantially below those in all commercial industries. Between 1951 and 1968, for example, the annual average rate of growth in productivity in commercial services was lower than it was in all commercial industries. Further, because the rate of price increase in government expenditures on goods and services was higher than consumer expenditures on services, it follows that productivity growth in the public sector (non-commercial services) was lower than in commercial services.

The explanation for the poor performance in the public sector in constraining price increases was a secular phenomenon. The shift from the production of goods to the production of services in terms of total output and employment has removed sizeable portions of the domestic economy from the restraints of international competitive forces. And when services are provided by non-commercial industries (government), the restraints of the domestic market are removed as well.

It does not follow that government is incapable of allocating resources efficiently within the public sector. A major trend in government over the past two decades has been the development of new techniques designed to measure needs, assign priorities and to allocate resources through expenditure programs. But the scanty evidence available suggests that the productivity record in the public sector has lagged, and that price increases have been excessive.

The experience of hospital insurance is indicative of the problems inherent in the shift from the private to the public sector. After the establishment of the hospital insurance program in 1959, the costs of hospital care rose rapidly. Commenting on this, the Ontario budget in 1961 stated:

“It should be pointed out that salaries and wages represent 70 per cent of the net operating costs of all public general hospitals and these have risen by 52.5 per cent in the last three years alone.”

The availability of tax revenues provided by the provincial and federal governments was one major factor in the escalation of hospital costs. It would, of course, be quite wrong to argue that this was the only factor influencing costs. But it was one factor, and an important factor in the sharp rise in hospital costs.

Education costs showed the same trend. As an increasing share of the total educational bill was absorbed by the provincial government, costs rose. Again it is not clear whether the availability of money led to excessive expenditures or whether enrolment accounts for the higher expenditures. The truth is probably that the relationship was circular—with a rising school population more money was needed, and the willingness of the province to accept a larger proportion of the educational bill stimulated spending by school boards, by universities and by the province itself.

The issue was not that there was real demand for expanded health and educational services. The issue was whether the political system was structured to maximize the benefits of rising expenditures, while at the same time encouraging the most efficient use of the available funds. On the grounds that the government enjoyed continued electoral success it could be argued that there was public support for rising expenditures on health and education. The question remained, however, of the extent to which the political process was an effective mechanism for the translation of public demand into precise spending priorities?

A conclusion that enjoys the benefit of hindsight is that rising government expenditures did not match a sufficient increase in productivity, so that they were inflationary in their impact on the economy. Given a better record in the allocation of resources at the disposal of the provincial government through improved productivity performance, the pressures of population growth created a situation that predicated the rapid expansion of provincial government expenditures.

Real net provincial expenditures rose at an annual average rate of 8.8 per cent between 1945 and 1971. In the same period, the population of Ontario increased at an annual rate of 2.5 per cent. Almost one third of the growth in provincial net spending was a direct consequence of overall population growth.

The impact of population growth was even more important than this figure indicates. There were four major contributing factors: immigration, migration, urbanization and the baby boom.

The inflow of almost two million persons into Ontario between 1946 and 1972 placed an unprecedented strain on government expenditures. In the main, the postwar arrival settled in the cities, and required urban services. Many of these services were provided by municipalities, school boards and other agencies of local government. But increasingly the province was required to help finance these services and this was reflected in the share of provincial expenditures paid to local governments.

Nor was the increase in the cost of government for urban services solely a function of immigration and migration from other provinces. Tens of thousands of people were moving off the farm and from rural Canada to the cities and towns of Ontario. Urbanization of the population was one of the major social and economic trends in the Fifties and Sixties. And this change in the location of the population was translated into rising government expenditures.

Urbanization has been one of essential factors influencing the growth of government expenditures at all levels. It is not just a question of size. It is a question of the range of services provided by government. Urban people demand a wide range of services—recreation, welfare, transportation and communications, housing, health and education, water and sewage waste disposal, and all the other urban services necessary to deal with huge agglomerations of people in an urban society. All of these reflect a qualitative as well as a quantitative expansion of the level of services provided in the public sector.

In this instance, it is not a question of what comes first, the people or the service. The emergence of metropolitan centres as a fact of life in Ontario has been directly responsible for a large part of the growth of provincial expenditures.

Of particular importance among the pressures on government expenditures arising from population growth was the age composition of the population. The baby boom from 1945 to 1960 created a special set of circumstances: the growth in demand for educational facilities. There was simply no escaping the implica-

tions of the rising number of school-age children. The schools had to be built and the teachers trained.

What can be questioned is whether the provincial response to this challenge was realistic in terms of the costs involved and the benefits received. Was the physical plant erected to meet the demand really needed? Was the best use made of the facilities provided? Was the whole system geared to the appropriate educational experience? Were there any substantial savings that could have been realized? Was too much done too fast? Whatever the answer, there can be no question that the unprecedented rise in the school-age population contributed directly to the growth in provincial government expenditures.

The third factor explaining the upsurge in provincial government spending was the expansion of government services.

Discounting both inflation and population growth, there remains a rate of increase in real net general expenditures per person annually of 6.1 per cent. This can be attributed to the expansion of government services. At this point the report is concerned with the evolution of economic and fiscal policy and the implications of this process. Other reports, dealing with social and resource and environmental policy, discuss the rise in expenditures in these policy fields.

TABLE I

Provincial Net General Expenditures
In Current and Constant Dollars

1945-1971

Fiscal Year	Calendar Year	Net Provincial Government Expenditure (\$ millions)	% Change	Deflator(1)	Net Real (1961 \$) Provincial Government Expenditures (\$ millions)	% Change
1945-1946	1945	132.3	-	45.4	291.4	-
1946-1947	1946	163.9	23.9	44.4	369.1	26.7
1947-1948	1947	201.1	22.7	47.8	420.7	14.0
1948-1949	1948	253.1	25.9	54.6	463.6	10.2
1949-1950	1949	282.8	11.7	58.4	465.9	.5
1950-1951	1950	305.4	8.0	60.7	503.1	8.0
1951-1952	1951	372.3	21.9	67.9	548.3	9.0
1952-1953	1952	404.6	8.6	71.0	569.9	3.9
1953-1954	1953	419.7	3.7	72.7	577.3	1.3
1954-1955	1954	441.3	5.1	75.6	583.7	1.1
1955-1956	1955	522.3	18.3	78.1	668.8	14.6
1956-1957	1956	592.3	13.4	83.5	709.3	6.0
1957-1958	1957	671.3	13.3	87.8	764.6	7.8
1958-1959	1958	750.1	11.7	90.4	829.8	8.5
1959-1960	1959	842.3	12.2	93.5	900.9	8.6
1960-1961	1960	871.6	3.4	96.8	900.4	-
1961-1962	1961	977.5	12.1	100.0	977.5	8.6
1962-1963	1962	1,106.5	13.2	102.4	1,080.6	10.5
1963-1964	1963	1,180.7	6.6	106.6	1,107.6	2.5
1964-1965	1964	1,305.5	10.5	110.3	1,183.6	6.9
1965-1966	1965	1,456.2	11.5	115.3	1,263.0	6.7
1966-1967	1966	1,791.1	23.0	123.1	1,455.0	15.2
1967-1968	1967	2,264.7	26.4	131.5	1,722.2	18.8
1968-1969	1968	2,745.4	21.2	139.0	1,975.1	14.7
1969-1970	1969	3,259.4	18.7	151.2	2,155.7	9.1
1970-1971	1970	3,851.8	18.1	160.5	2,399.9	11.3
1971-1972	1971	4,262.5	10.7	170.7	2,497.1	4.0

Sources: Smith Committee Report; Various Provincial Budgets (1967-1972); Revised National Accounts, 1972

(1) Implicit Price Index - Government Expenditures on Goods and Service, 1967=100

TABLE II

Relationship Between Population
and Net General Expenditures
Per Capita

1945-1971

Calendar Year	Population (000's)	% Change	Net Expenditure per capita	% Change	Net Real Expenditures per capita	% Change
1945	4,000	-	33	-	73	-
1946	4,093	2.3	40	21.2	90	23.3
1947	4,176	2.0	48	20.0	101	12.2
1948	4,275	2.4	59	22.9	108	6.9
1949	4,378	2.4	65	10.0	106	- 1.9
1950	4,471	2.1	68	4.6	113	6.6
1951	4,598	2.8	81	19.0	119	5.3
1952	4,788	4.1	84	3.7	119	-
1953	4,941	3.1	85	1.2	117	- 1.7
1954	5,115	3.5	86	1.2	114	- 2.6
1955	5,266	2.9	99	15.1	127	11.4
1956	5,405	2.6	110	11.1	131	3.1
1957	5,636	4.2	119	8.2	136	3.8
1958	5,821	3.3	129	8.4	143	5.1
1959	5,969	2.5	141	9.3	151	5.6
1960	6,111	2.4	143	1.4	147	- 2.7
1961	6,236	2.0	157	9.8	157	6.8
1962	6,351	1.8	174	10.8	170	8.3
1963	6,481	2.0	182	4.6	171	.6
1964	6,631	2.3	197	8.2	178	4.1
1965	6,788	2.4	215	9.1	186	4.5
1966	6,961	2.5	257	19.5	209	12.4
1967	7,127	2.4	318	23.7	242	15.8
1968	7,262	1.9	378	18.9	272	12.4
1969	7,385	1.7	441	16.7	292	7.4
1970	7,551	2.2	510	15.6	318	8.9
1971	7,703	2.0	553	4.5	324	1.9

Sources: Smith Committee Report; Various Budgets, 1967-1972

TABLE III

Relationship Between Personal Income and Net General Expenditures

1945-1971

Calendar Year	Personal Income (\$ million)	% Change	Personal Income per capita	% Change	Deflator(1)	Real Personal Income per capita	% Change	Net Real Government Expenditures as % of Real Income per capita	Net Government Expenditures as % of Personal Incomes
1945	3,722	-	931	-	58.2	1,600	-	4.6	3.6
1946	3,805	2.2	930	-	60.2	1,545	-3.6	5.8	4.3
1947	4,235	11.3	1,014	9.0	65.7	1,543	- .1	6.5	4.7
1948	4,851	14.5	1,135	11.9	74.6	1,521	-1.4	7.1	5.2
1949	5,199	7.2	1,188	4.7	77.3	1,537	1.0	6.8	5.4
1950	5,638	8.4	1,261	6.1	79.7	1,582	2.9	7.1	5.4
1951	6,521	15.7	1,418	12.5	87.8	1,615	2.1	7.4	5.7
1952	7,207	10.5	1,505	6.1	89.8	1,676	3.8	7.1	5.6
1953	7,681	6.6	1,555	3.3	89.6	1,735	3.5	6.7	5.5
1954	7,930	3.2	1,550	-.3	90.5	1,713	-1.3	6.7	5.6
1955	8,525	7.5	1,619	4.5	90.5	1,789	4.4	7.1	6.1
1956	9,320	9.3	1,724	6.5	92.0	1,874	4.8	7.0	6.4
1957	10,211	9.6	1,812	5.1	94.9	1,909	1.9	7.1	6.6
1958	10,802	5.8	1,856	2.4	97.3	1,908	-	7.5	6.9
1959	11,406	5.6	1,911	3.0	98.4	1,942	1.8	7.8	7.4
1960	11,923	4.5	1,951	2.0	99.4	1,963	1.1	7.5	7.7
1961	12,187	2.2	1,954	.2	100.0	1,954	-.5	8.0	8.0
1962	13,098	7.5	2,062	5.5	101.4	2,034	4.1	8.4	8.4
1963	13,976	6.7	2,156	4.6	102.9	2,095	3.0	8.2	8.4
1964	15,030	7.5	2,267	5.1	104.2	2,176	3.8	8.2	8.7
1965	16,537	10.0	2,436	7.5	106.3	2,292	5.3	8.1	8.8
1966	18,655	12.8	2,680	10.0	109.7	2,443	6.6	8.6	9.6
1967	20,553	10.2	2,884	7.6	113.5	2,541	4.0	9.5	11.0
1968	22,844	11.1	3,146	9.0	118.2	2,662	4.7	10.2	12.0
1969	25,638	12.2	3,472	10.4	122.8	2,827	6.2	10.3	12.7
1970	27,874	8.7	2,691	6.3	126.9	2,909	2.9	10.9	13.8
1971	30,560	9.6	3,967	7.5	129.7	3,059	5.1	10.6	13.9

Sources: Revised National Accounts, 1972; Smith Committee Report; Various Budgets, 1967-1972

(1) Implicit Price Index—Consumer Expenditures on Goods and Services

TABLE IV

Percentage Distribution of
Provincial Net General Expenditures
by Functional Classification

1945-1970

Year	Education	Health	Welfare	Highways	Natural Resources	Law Enforcement	Municipal Affairs	Public Works
1945	21.3	10.6	10.6	15.2	8.0	3.8	5.3	1.0
1946	24.4	9.8	9.8	17.1	7.9	4.7	2.5	1.1
1947	20.8	8.2	8.2	27.7	7.6	3.8	2.1	1.6
1948	20.6	6.8	6.8	30.8	6.8	4.1	1.8	2.7
1949	19.5	7.0	7.0	26.8	6.9	4.5	1.6	3.0
1950	19.1	7.7	7.7	25.5	7.3	4.0	1.4	3.2
1951	19.9	7.8	7.8	26.9	6.0	4.0	1.5	3.9
1952	19.1	6.6	6.6	27.4	5.2	4.6	1.4	3.3
1953	19.7	5.4	5.4	29.7	5.1	4.0	1.9	3.1
1954	20.5	5.7	5.7	27.2	4.7	4.1	2.2	5.3
1955	21.8	5.9	5.9	25.0	4.3	4.3	4.2	6.0
1956	20.1	5.2	5.2	30.0	4.7	4.2	3.0	5.8
1957	19.1	5.0	5.0	33.4	4.0	3.8	2.9	6.0
1958	22.0	5.4	5.4	31.9	4.2	4.0	3.8	7.5
1959	24.5	5.6	5.6	30.6	4.0	4.0	3.7	6.6
1960	25.2	5.3	5.3	29.8	4.0	4.1	3.9	5.9
1961	27.0	5.9	5.9	27.5	3.8	3.9	4.2	4.8
1962	27.7	5.6	5.6	25.1	3.8	3.7	4.0	4.1
1963	32.3	5.1	5.1	22.8	3.5	3.6	3.8	3.4
1964	33.1	5.1	5.1	23.8	3.6	4.1	3.8	3.4
1965	35.2	5.8	5.8	23.1	3.3	4.0	3.2	3.4
1966	37.1	5.1	5.1	21.9	3.5	4.0	2.8	3.5
1967	40.1	4.1	4.1	18.7	3.3	4.4	3.1	3.1
1968	39.7	4.1	4.1	16.0	3.3	4.9	6.9	3.0
1969	40.8	3.6	3.6	13.9	3.0	4.6	6.3	2.6
1970	40.9	3.6	3.6	13.2	2.9	4.2	6.5	3.4

Source: 1945-1964—The Ontario Committee on Taxation Report Volume 1.
1965-1971 Budget Statements

Note: The data from 1965 to 1971 are not directly comparable to the date from the earlier period because of changes in accounting systems and reorganization of government.

Problems and Implications

The gradual evolution of provincial economic policy from the passive financial policy of the early 1950's to the full expression of a positive fiscal policy of the late 1960's has brought a new set of problems to the forefront of public debate. The central issue is the coordination of economic policy within a multi-level system of government.

There are, flowing out of this central issue, four related problems:

1. The establishment of agreement on economic policy objectives.
2. The rational division of responsibility by level of authority for the execution of programs designed to achieve the agreed policy objectives.
3. The creation of the essential coordination mechanisms to ensure the compatibility of revenue and expenditure decisions taken at each level.
4. The appropriate allocation of revenue resources to each level of government.

How far has Ontario come in resolving these problems?

Economic Policy Objectives

On the surface there would seem to be general agreement on the economic policy objectives of full employment, rising incomes, stable prices, a viable balance of payments and a more equitable distribution of income.

The Ontario government, particularly in the decade of the Sixties, geared its expenditure and revenue policies towards the attainment of economic growth, full employment and rising incomes. Even though it had no direct influence upon monetary policy, the province restrained expenditure increases in the 1969 budget to assist in controlling inflation.

The province's priorities in health, education, welfare and housing suggest that it was vitally concerned with effecting a more equitable distribution of incomes.

What then were the sources of conflict?

First and foremost was the disagreement over priorities. The problem with stated national economic goals is that they are not mutually consistent and they are subject to divergent interpretations.

A series of federal initiatives included the dropping of the Technical and Vocational Training Agreement and its replacement by the Manpower Training Act, the creation of the Department of Regional Economic Expansion, the moves in the consumer affairs and securities areas, tax reform, medicare, the unwillingness to negotiate on tax-sharing, the fight against inflation, and certain proposed amendments to social security legislation. These created an environment of distrust between the province and Ottawa, as being conceived and executed on a unilateral rather than a multilateral basis.

The apparent agreement on objectives, therefore, without a parallel understanding on priorities, policy mechanisms, and timing, has not been reflected by a mutuality of effort to achieve common goals. The national economic objectives were deficient because they did not assign priorities to the several goals, nor did they indicate how or by whom they would be achieved. Rather than leading to understanding and agreement, they have contributed to discord and conflict.

The situation was complicated even further by the growing concern that the economic policy objectives set out by the Economic Council of Canada in 1963 were inadequate as goals of public policy.

The pursuit of growth has led to massive foreign investment and foreign ownership of key sectors of the economy. The debate on foreign ownership had given an entirely new dimension to the economic policy question. The economic objectives did not provide any guidance.

The environmental issue and the demand for an “improved quality of life” raised yet another dimension to economic policy. There is now general agreement that the national accounts system of measurement of economic development is inadequate. Yet there was no other measure available with the same utility or acceptance.

Beyond this technical question was the broader issue of the validity of the proposition that economic growth was itself a valid measure of social welfare or progress. Again the question was raised whether economic goals were appropriate as the ultimate yardstick of public policy. This represented a fundamental challenge to the ideology that had dominated public policy formulation in the postwar era.

The Division of Responsibility

Jurisdictional responsibility under the British North America Act has been and remains one of the major unresolved areas of the Canadian federal system.

The device that has been used extensively over the past twenty-five years, conditional grants within shared-cost programs, has proven unacceptable on several grounds. During the period of “cooperative federalism,” the shared-cost programs proliferated until virtually every area of government activity involved at least two and often three levels of government. The complex system that evolved was inadequate not only because of inherent inefficiencies, but because political problems were created when responsibility was diffused through several levels of government.

Shared-cost programs have been criticized on such grounds as that they distorted spending priorities, they limited central

control over expenditures, they tended to be universalistic in application rather than specific, they favoured the richer provinces at the expense of the poorer provinces, they infringed on the constitutional powers of provincial governments. The list of real or alleged complaints could be extended.

The crux of the problem lay in the Canadian constitution. The nature of modern urban society places the primary emphasis on those governmental functions assigned to the provinces under the British North America Act, which was not designed nor intended for the Canadian economy of today. Yet only a few of the provinces have the population and financial base, together with the essential administrative sophistication, to deal with the realities of urban-industrial life. The incongruities of the provincial system have been the basis for a continuing imbalance in the federal framework.

The shared-cost approach was evolved to meet the problems inherent in the provincial disparities in population and wealth. As long as Canadians insisted on the integrity of out-dated provincial boundaries and provincial autonomy, the inevitable course seemed to be some form of indirect federal involvement in "provincial" matters.

The failure of shared-cost programs to achieve a commonality of standards between provinces was also related to fundamental disparities among ten provinces. Without built-in equalization factors, the conditional grant approach was inadequate. And even with the equalization payments, outside of the conditional grant system, the variation in problems, in administrative competence, in perception of needs, militated against the universalistic approach of the shared-cost program.

The inadequacies of the shared-cost program have been recognized increasingly over the past decade. One result has been the halting, but gradual, progress towards constitutional reform. Without this, the chances for a viable federal system in Canada are diminished. The political system is now virtually incapable of handling emergent problems within the old framework. Something new is needed.

The Ontario position vis-à-vis the federal government is symptomatic of the growing malaise in the whole system. It is not just a question of a lack of cooperation. It is more the failure of the

existing federal system to cope with problems that fall outside of the constitutional framework provided more than a century ago in the B.N.A. Act.

The same problems are inherent in provincial-municipal relations. Here, however, the legal subordination of the municipalities to the province has led to more flexibility in approach, and the province in many areas (pollution controls, administration of justice, assessment) has simply taken over the function or created special-purpose bodies.

The reorganization of municipal government became an established policy of the Ontario government. It would not be too surprising if the reorganization takes a very long time and results in a municipal system quite different from that now anticipated. The province's record in municipal reform has not been impressive if measured in terms of time. It should be remembered that the major plan of the government in 1943 was the reform of the municipal tax base. Some thirty years later the reform is still not resolved.

Coordinating Mechanisms

The reality of the constitutional crisis is not to be found in the demise of the so-called "Victoria Charter". It is to be found in the on-going plethora of committees, conferences, meetings and discussions between the federal and the provincial governments.

The truth of the matter is that Canada has evolved a new level of government, a federal-provincial government. It has no constitutional basis. It has no legislative authority. It has no directly elected body. But, it has a growing bureaucracy. More and more officials are devoting more and more time to the work involved in intergovernmental relations.

This is a key fact of government in the Canadian federal system. But, in the absence of a formal legislative structure, administrative cooperation and coordination have operated in a vacuum.

The need for a more complex system of intergovernmental relations has arisen in the proliferation of shared-cost programs. Whenever two or more governments were involved in a program, some form of integrated administrative mechanism was needed. And when some provinces began to move towards comprehen-

sive economic and regional planning, expressed through a provincial fiscal policy, it was essential that some mechanisms for coordination should be constructed.

To date, however, the record has not been adequate. Cooperation at the administrative level is not enough. In the absence of political commitments, and without some formal methods of translating agreements into binding legislation, the coordination of fiscal policy cannot be achieved.

Although the Canadian system has proceeded on an ad hoc basis in many areas and with many programs, the ultimate political sanctions have been missing. It lacks any institutional device. Constitutionally, the provinces and the federal government retain sovereignty over those areas of legislative competence assigned to them under the B.N.A. Act. Agreement between the two levels takes on the appearance of treaties, but without the formality of ratification.

Canada's federal system has reached a crucial point in its evolution. The central question is where does it go from here? Will the pendulum swing back to centralization of control at the federal level? Or will the provinces, at least some of them, press for more freedom of action under the banner of "fiscal integrity"?

Tax-Sharing

Much of the heat of debate on federal-provincial matters is generated by the continuing argument of the festering sore of Canadian federalism—the allocation of revenue resources.

The Ontario position on tax-sharing has changed in parallel with its position on fiscal policy. As the province has expanded its expenditures many times for reasons beyond its control, it has had a growing need for a larger share of tax revenues. And, as the province has related its expenditures to its fiscal requirements, it has recognized the need not only for a greater share of the direct tax field, but also the need to use tax policy as an independent fiscal tool.

The discussion of the changing perception of the province's role in economic policy and its changing appreciation of provincial fiscal policy, highlights the current dilemma. Faced with a federal government that refuses to negotiate on tax-sharing and

enacts a centralizing tax reform bill, the province has been forced to raise its ante in the political poker game. Whether it desires a provincial income tax or not, it has been forced into this possibility by the pressure of events.

In the absence of a new understanding with Ottawa, and without a fundamental reform of political institutions, the province finds itself involved in a no win game. It can either capitulate and give up control over provincial economic development, or it can attempt to push forward provincial policies without regard to the federal implications. Neither alternative is politically acceptable nor economically sensible in the long-run.

The Limitations of Provincial Fiscal Policy

Total provincial and municipal government spending in Canada now surpasses federal spending. In 1957, for example, federal expenditures (excluding transfer payments) accounted for 14.3 per cent of Ontario's Gross Provincial Product and provincial-municipal spending for 10.3 per cent. By 1969, the positions had been reversed with the provincial-municipal partnership accounting for 18.8 per cent of Ontario GPP and federal spending for only 12.6 per cent.

In addition, it has been estimated that some 49 per cent of total federal spending is statutory expenditure resulting from existing legislative commitments, many of them tied to conditional grants. Thus the federal government operates within real restraints in adopting a fiscal policy.

At the provincial level, the government finds itself caught in a two-way squeeze. At least 60 per cent of the province's net general expenditures are locked into shared-cost programs with the federal government on one side and the municipal governments on the other.

Total federal transfer payments represented slightly more than 20 per cent of provincially generated revenues in 1968. Of the \$603 million transferred to the province from Ottawa in 1968-69, \$476 million were in the form of conditional grants. This represented 17 per cent of provincial net expenditures. In 1971-72 of the \$1,101 million transferred, \$1,096.3 million was in the form of conditional grants, which represented 25.7 per cent of provincial net expenditures.

At the other end of the scale, provincial-municipal transfers have become even larger. In 1968-69, for example, transfer payments from the province to the municipalities accounted for 43 per cent of net provincial expenditures and more than 85 per cent of these transfers were conditional grants. In 1971-72 transfer payments accounted for 41.1 per cent of net provincial expenditures of which 94.8 per cent were conditional grants.

The significance of shared-cost programs is that a level of government is restricted in establishing revenue but not spending priorities. Almost every decision must be made in the context of the existing grants system. By locking in such a large proportion of their expenditures into conditional grants, the federal and provincial governments have lost flexibility on the expenditure side and restricted their freedom of action on the revenue side of fiscal policy.

Another related problem has been the need to expand provincial spending to meet new priorities without a compensating cut-back on programs financed in part by conditional grants. This might well have been the real distortion in provincial priorities caused by the existence of shared-cost programs.

In any case, the financial and constitutional framework within which the province operated restricted the implementation of a purely provincial fiscal policy.

Overloading

Given the problems associated with the development of a provincial fiscal policy designed to implement a provincial economic policy, a final problem may be seen to be emerging. For Ontario is the existence of a comprehensive set of provincial economic goals possible? It may be mentioned that the electorate of Ontario is well represented in the federal Parliament, and an effort may be possible to influence the votes of Ontario M.P.'s on behalf of provincial objectives. Such an effort remains to be tried.

The 1971 budget contained a statement of provincial objectives for fiscal policy:

“to restore full-employment economic growth in Ontario by encouraging expansion of the activities of the private sector;

“to maintain firm control over public spending in order to contain tax levels and the generation of inflationary pressures;

“to advance provincial-municipal reforms in line with the long-term program we announced in 1969; and

“to ensure the attainment of the other priorities of government policy such as greater Canadian participation in our economic life, preservation and conservation of the environment, and a fulfilling quality of life for all our citizens.”

The question that emerges is whether the province, in fact, can achieve all of these objectives within a fiscal policy operating under the existing restraints? Or, is Ontario trying to do too much under the umbrella of fiscal policy? Finally, are the “other priorities of government policy” achievable through fiscal policy at all?

This is the problem of overloading. The province, in its desire to present a comprehensive package in the budget statement, has moved from a budget that spells out the policy and then attempts to reconcile the financial implications to a budget that sweeps all policy under the general heading of fiscal policy. This raises the issue of what fiscal policy really is? Is it the financial plan of government or is it the ultimate expression of governmental policy?

Certainly, at least since 1967, the fiscal policy of Ontario has attempted to be the total expression of government policy. But the question remains, does this forcing of all policy into the framework of revenues and expenditures do justice to the reality of the political process? Or is the fiscal policy of the province simply one factor, albeit an important factor, in the total effort of government in shaping the future of the province?

In conclusion, the period in Ontario's history since World War II may be seen as one of profound transformation in the Canadian political system. The economic transformation of Ontario has been far-reaching and an analysis of events in the recent past leads inevitably to considerations of the proper social and economic goals for the future. Such considerations must, of course, be tempered by an understanding of the past.

A major shift in government has occurred in Ontario. It is no longer purely administrative in character. It has developed its own planning orientation, and the change has by no means run its course. The nature and the purpose of government, as far as Ontario is concerned, have undergone profound alteration. Ontario's experience undoubtedly has its counterparts in other provinces. The study and report upon the state of Confederation may well preoccupy many Canadian minds in the years ahead. The task may be defined as one by which Canadians will optimize the future of their country.

HC Richmond, D.R.
117
.06 The economic
.0685 transformation of Ontario.
no.1

REFERENCE CUT 1

Ontario Ministry of Treasury, Economics
and Intergovernmental Affairs Library
FROST BUILDING QUEEN'S PARK
TORONTO, ONTARIO, CANADA

Ontario Ministry of Treasury, Economics
and Intergovernmental Affairs Library
FROST BUILDING QUEEN'S PARK
TORONTO, ONTARIO, CANADA

